15 T.C. 989 (1950)

An election to receive a reduced annuity in exchange for a survivor annuity for a designated beneficiary is not a transfer subject to estate tax inclusion under Section 811(c) of the Internal Revenue Code when the decedent retained no reversionary interest.

Summary

The Tax Court addressed whether a decedent's election to receive a reduced annuity in exchange for a survivor annuity for his former wife constituted a transfer includible in his gross estate under Section 811(c) of the Internal Revenue Code. The decedent, after 30 years of foreign service with Standard Oil, elected a reduced annuity, with the balance to be paid to his former wife if she survived him. The court held that this election was not a transfer under which the decedent retained possession, enjoyment, income rights, or a reversionary interest, thus the annuity was not includible in his estate.

Facts

Frederick Twogood worked for Standard Oil of New York and its successors for 30 years in China. He was interned by the Japanese during World War II, later released, and retired on July 1, 1943. Prior to retirement, on October 15, 1937, Twogood elected under the company's pension plan (Group Contract No. 103) to receive a reduced monthly annuity of $955.82 instead of $1,073.34. He designated his then-wife, Theresa, as the beneficiary of a $416.67 monthly annuity if she survived him. A separation agreement in 1938 obligated Twogood not to change this designation. Twogood died on April 28, 1944; Theresa began receiving the survivor annuity.

Procedural History

The estate tax return was filed, and the tax paid. The Commissioner of Internal Revenue added $107,945.59 to the gross estate, representing the value of the annuity payable to Twogood's former wife, arguing that Twogood made a transfer under Section 811(c). The Tax Court heard the case on November 30, 1949, after an amendment to Section 811(c) was approved on October 25, 1949.

Issue(s)

Whether the decedent made a transfer within the meaning of Section 811(c) of the Internal Revenue Code by electing to receive a reduced annuity so that his former wife would receive an annuity if she survived him, and whether that transfer is includable in his gross estate.

Holding

No, because the decedent did not retain the possession or enjoyment of the

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transferred property, the right to income from it, or a reversionary interest in the property, as required by Section 811(c) as amended by P.L. 378 (1949).

Court's Reasoning

The court reasoned that Twogood's election was a division of property rights – his future annuity benefits – into two parts. He retained one part as a reduced annuity and transferred the other to his beneficiary, contingent on her surviving him. The court analyzed Section 811(c), concluding that the transfer was not made in contemplation of death under Section 811(c)(1)(A). Furthermore, under Section 811(c)(1)(B), Twogood did not retain possession, enjoyment, or the right to income from the transferred property; the annuity payments he received were separate from the transferred portion. Most importantly, the court applied Section 811(c)(2), which requires a reversionary interest for the transfer to be included in the gross estate under Section 811(c)(1)(C). Since Twogood retained no such interest, the annuity was not includable. The court distinguished its prior holding in *Estate of William J. Higgs*, noting that the Third Circuit reversed *Higgs*, reasoning that Twogood's annuity was the result of the contract between his employer and the insurance company, not a transfer by Twogood himself. As the court stated, "The annuity which the decedent had was the inevitable result, not of the incidental exercise of the option, but of the contract which was arranged by and between his employer and the insurance company pursuant to which he was entitled to an annuity in any event."

Practical Implications

This case clarifies the application of Section 811(c) to annuity elections, particularly in the context of employer-provided pension plans. It establishes that simply electing a survivor annuity does not automatically trigger estate tax inclusion. The key factor is whether the decedent retained any control or reversionary interest in the portion of the annuity transferred to the beneficiary. The case also highlights the importance of the 1949 amendment to Section 811(c), which explicitly required a reversionary interest for transfers intended to take effect at death to be included in the gross estate. Later cases must consider the specific terms of the annuity plan and whether the decedent had any possibility of the transferred benefits reverting to them or their estate. It shows the importance of examining the source of the annuity contract and whether the decedent actually transferred property to purchase the annuity.

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